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FM AMCONSUL SHANGHAI
TO RUEHC/SECSTATE WASHDC PRIORITY 7199
INFO RUEHBJ/AMEMBASSY BEIJING PRIORITY 2153
RUEATRS/DEPT OF TREASURY WASHINGTON DC
RUCPDO/DEPT OF COMMERCE WASHINGTON DC
RUEHGZ/AMCONSUL GUANGZHOU PRIORITY 1407
RUEHHK/AMCONSUL HONG KONG PRIORITY 1591
RHEHAAA/NSC WASHINGTON DC
RUEHSH/AMCONSUL SHENYANG 1430
RUEHCN/AMCONSUL CHENGDU 1436
RUEHGH/AMCONSUL SHANGHAI 7786

UNCLAS SHANGHAI 000419

SENSITIVE
SIPDIS

TREASURY FOR OASIA-DOHNER, HAARSAGER, CUSHMAN, WINSHIP
USDOC FOR ITA DAS KASOFF, MELCHER, OCEA
NSC FOR LOI

E.O. 12958: N/A

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SUBJECT: AIG FACING FURTHER REGULATORY PRESSURE

1. (SBU) Summary: A top AIG official in China on September 25 described disruptive new reporting requirements from the China Insurance Regulatory Commission (CIRC). These are having a significant impact on AIG's operations in China, and AIG is working with regulators to institute more workable compromise measures. End summary.

CIRC's New Reporting Requirements

2. (SBU) A top AIG official based in Shanghai told Congen Econoff that as of Monday, September 22, AIG was complying with a new CIRC demand that AIG provide the regulator with daily updates of its financial accounts, and also to get pre-approval from CIRC for all movement of capital out of China. The AIG official said that CIRC's intention apparently is two-fold: (1) To assure that no AIG capital is improperly sent to the parent company, and (2) to assure that AIG capitalization is adequate to pay claims in China. CIRC presented the new procedure to AIG on Friday, September 19, and AIG consulted with its legal department before complying on Monday, September 22.

3. (SBU) The AIG official said that CIRC most likely is reacting to New York State's recent regulatory changes allowing the parent company to access the capital of subsidiaries in the New York area, which was intended to help resolve AIG's liquidity problems. (Note: According to U.S. financial press, New York Governor David Patterson announced on September 15 that AIG would be allowed to use \$20 billion of its subsidiaries' holdings as collateral to borrow cash. End note.) The Shanghai-based AIG official said that recent concerns in the United Kingdom over a Lehman funds transfer from a U.K. subsidiary to the parent company may also have played a role.

Significant Impact on AIG's Business

4. (SBU) These new requirements are having a significant impact on AIG's daily operations in China, said the AIG official. Normally, AIG's China operations make multiple movements of funds to the United States, including for payment of claims by U.S.-based policyholders and for payments to U.S.-based reinsurers. Under the new requirements, AIG must provide CIRC with details of planned capital transfers every day at around 4 o'clock, and then wait for CIRC's approval before proceeding. In itself, this is a burden to AIG's operations. In addition, CIRC has stopped two transactions from proceeding, and there is no indication of when these transactions will be approved.

5. (SBU) AIG is working with Yuan Li, CIRC Assistant Chairman,

and with the local Shanghai insurance regulator to reach a more workable compromise, said the AIG official, but there is no indication that CIRC will accept one. Specifically, AIG would prefer to set a limit under which AIG would be allowed to transfer funds overseas without preapproval from CIRC, say around RMB 1 million. These would still be included in the daily financial report, in the AIG offer, while transfers over that amount would still be subject to prior approval.

Are AIG's China Operations For Sale?

¶5. (SBU) The AIG official further noted that at a recent internal meeting between CIRC and Chinese insurance companies, CIRC had inquired about the impact of AIG's financial issues on the domestic firms. In addition, CIRC had raised the subject of whether a domestic insurer would be interested in or willing to purchase AIG's assets in China. According to the AIG official, one company indicated it was in a position to make the deal. The AIG official noted, though, that AIG almost certainly would not be interested in selling its China business, especially considering the firm's historical ties with China. (Note: AIG was actually founded in Shanghai. End note.)

Comment

¶6. (SBU) CIRC's new daily regulatory oversight over a foreign insurer provides a window on the regulatory measures that China may be considering in other business sectors as the financial crisis continues. The AIG official suggested that this Chinese measure was modeled after a similar one imposed on AIG operations in Hong Kong, which also strikes us as a likely pattern for potential future Chinese regulatory steps.

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